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# Oversight of HMRC soft law: lessons from the Ombudsman

## The ombudsman, tribunals and administrative justice section

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### ABSTRACT

An investigation of the role which the Ombudsman plays in tax law, on which comparatively little has been written, reveals that the body makes an important and distinct contribution. There is now almost universal acceptance that tax law is overly complex and indeterminate. If the primary law offers few answers to the taxpayer, then HMRC's role as administrator of the system becomes apparent. Soft-law elaborating upon how HMRC will apply the primary law to a given class of taxpayers is rendered indispensable. In practice however, HMRC soft-law has often been found to be deficient. Analysis of the current oversight arrangements for HMRC soft-law immediately reveals the genesis of these issues. Select committees exercise Parliamentary control, whilst an independent body performs external audits. These entities however only incommensurately examine the soft-law. Into this void steps the Parliamentary and Health Service Ombudsman, a body which has 'carved for itself a distinctive niche' in the public law framework. The paper accordingly seeks to elaborate upon the important role that the Ombudsman plays in scrutinising HMRC soft-law and the lessons which can be derived from this analysis.

KEYWORDS: Ombudsman; tax law; public law; soft law

## **Introduction**

An investigation of the role which the Parliamentary Ombudsman plays in tax law, on which comparatively little has been written, reveals that the body makes an important and distinct contribution. There is now almost universal acceptance that tax law is overly complex and indeterminate. If the primary law offers few answers to the taxpayer, then the role of Her Majesty's Revenue and Customs (HMRC) as administrator of the system becomes apparent. Soft-law elaborating upon how HMRC will apply the primary law to a given class of taxpayers (Mowbray, 1987, p. 572) is rendered indispensable. In practice however, HMRC soft-law has often been found to be deficient. Analysis of the current oversight arrangements for HMRC soft-law immediately reveals the genesis of these issues. Being a non-ministerial body, the traditional elements of individual ministerial responsibility are eschewed. Control is not effectuated at a ministerial level and so accountability must be sought through alternate avenues. To this end, select committees exercise Parliamentary control, whilst an independent body performs external audits. These entities however incommensurately examine the soft-law.

Into this void steps the Parliamentary and Health Service Ombudsman (Ombudsman), a Nordic import (CK Allen, 1962, p. 610) whose own inception is owed to perceived deficiencies in the existing apparatus for scrutinising executive action. The original purpose of the office was to act as an aid to Parliamentary scrutiny of the executive, (Abraham, Preface to Kirkham, 2007, p. 1) the other supervisory mechanisms such as questioning by MPs in Parliament and indirect oversight by the courts having been deemed to be insufficient for the task (Leyland and Anthony, 2012,

p. 125). Former Ombudsman Ann Abraham has opined however that the role of the office is now much broader than originally conceived and that the office acts ‘as a source of dispute resolution, as a guardian of good public administration, and as a systematic check upon departmental effectiveness’ and as such, has ‘carved for itself a distinctive niche’ in the public law framework (Abraham, Preface to Kirkham, 2007, p. 1).

The paper accordingly seeks to elaborate upon the important role that the Ombudsman plays in scrutinising HMRC soft-law and the lessons thereafter which can be derived from this analysis. Although it will ultimately be concluded that the Ombudsman is not the one-size-fits-all solution to the deficiencies in oversight of HMRC soft-law, it will be argued that the body nevertheless plays a unique constitutional role, one which should be interwoven alongside other institutional solutions. The paper will firstly sketch out the inutility of the traditional mechanisms for oversight of HMRC, namely, the House of Commons Treasury Committee (TSC) and the House of Commons Public Accounts Committee (PAC), National Audit Office (NAO), and Comptroller and Auditor General (CAG). The second part analyses the problems which proliferate in relation to HMRC soft-law, namely insufficiency of clarity, consistency with the law, and publication. The third part assesses the contribution that the Ombudsman has made to the scrutiny of HMRC soft-law.

### **Scrutiny of HMRC soft-law by the formally empowered bodies**

HMRC soft-law is not subject to any formalized system for review. As HMRC is a non-ministerial governmental department, Parliamentary oversight is exercised through channels alternate to those traditionally associated with ‘individual ministerial responsibility’. The most powerful of these channels are the select committees, the

formal vehicles through which scrutiny of HMRC is to take place. However, although both the TSC and the PAC have nominal jurisdiction over soft-law issued by HMRC, neither has in fact chosen to exercise such a role. Whilst it will be revealed that the TSC has neglected to pay attention to soft-law in general, a case study of the PAC's scrutiny of Extra-statutory concessions will be utilised to demonstrate that even where the body has been specifically designated a task of supervising HMRC soft-law, it has been inadequate in doing so.

### ***TSC***

The TSC is appointed by the House of Commons to examine the expenditure, administration and policy of HM Treasury, HMRC, and associated public bodies (Standing Order No.152, Standing Orders of the House of Commons, 2015). It was established in 1979 under the title of 'The Treasury and Civil Service Select Committee' and owes its genesis to the Procedure Committee, which recommended the introduction of committees (Select Committee on Procedure 1978). The object was to rationalize the system for parliamentary scrutiny of government departments. Analysis of the TSC's relationship with HMRC reveals however that the practise of the body is concerned more broadly with aspects of administration, policies undertaken and value-for-money, rather than the scrutiny of the substance of soft-law promulgated by HMRC.

For instance, during the 2010-15 Parliamentary session, the TSC concerned itself with the circa 6 million under and overpayments of tax revealed in September 2010 (TSC, 2011), the tax gap (the difference between tax paid and tax owed according to HMRC) and questioning of Dave Hartnett over an apparent 'sweetheart settlement' with Goldman Sachs (TSC, 2012) and the operation of the PAYE system (TSC, 2010). Additionally, Lin Homer (Chief Executive of HMRC) produced a letter for the TSC

with information concerning the publication of HMRC's Business Plan 2014-16 (Homer, 2014), whilst the TSC also held an inquiry into potential tax evasion via Swiss HSBC accounts (TSC, 2015). Meanwhile, over the course of the 2005-2010 session, the TSC inquired of the closure and movement of offices, relationship with Mapeley STEPS, staff morale (TSC, 2008a), child trust funds (TSC, 2008b), administration issues (such as data security (TSC, 2008c) and tax credits (TSC, 2007a)), expenditure (TSC, 2006; TSC, 2005), and the merger of the Inland Revenue and Customs and Excise departments (TSC, 2007b).

In contrast to all this scrutiny, an analysis of 10 years of TSC reports reveals that at no stage did the TSC review the adequacy of soft law made within the HMRC.

### ***CAG, NAO, and PAC***

The CAG, NAO and PAC operate an interrelated supervisory role over HMRC. The CAG carries out examinations into the economy, efficiency and effectiveness with which governmental departments have used their resources in discharging their functions (National Audit Act 1983, s. 6(1)). The officeholder accordingly has considerable discretion to decide what areas of tax administration to examine (National Audit Act 1983, s. 1(3)), although the primary function since the office's inception in 1866 has been to examine accounts on behalf of the House of Commons (McEldowney, 2011, p. 357). The CAG is head of the NAO (National Audit Act 1983, s. 3(1)(a)), and an officer of the House of Commons (National Audit Act 1983, s. 1(2)). Being an auditor, the NAO's primary function is executed by way of auditing the financial statements of government departments and evaluating value-for-money of public spending (McEldowney, 2011, p. 356). The NAO also carries out investigations into areas of concern, as with the report into the settling of large tax disputes by HMRC

(NAO, 2012). Additionally, the body acts on an international level, for instance carrying out external audits for other international organisations (Daintith and Page, 1999, p. 194). The NAO also supports the services of Parliament, by presenting its reports to the PAC (Daintith and Page, 1999, p. 197), which, like the TSC, is a select committee of the House of Commons. Most reports of the NAO and CAG are used as the basis of PAC hearings (McEldowney, 2011, p. 356; Cane, 2011, p. 368).

Unlike the TSC, whose role *prima facie* overlaps with the triumvirate of the CAG, NAO and PAC (McEldowney, 2011, p. 356), the three entities have a distinct mandate apropos soft-law, specifically extra-statutory concessions (ESCs), traceable back to a Treasury Minute from 1897 (PAC, 1898, pp. 147-148). The regime through which ESCs are decided is an example of an area of tax law delivered through soft law. By way of brief background, ESCs grant to taxpayers relief or a reduction in tax liability to which they are not strictly entitled (HMRC, 2014, p. 4). These concessions may apply to individuals or classes of taxpayers and in the case of the latter, may or may not be published. At the end of the 19th century, the Bank of England held part of the estate of Alexander III of Russia and this concession attempted to exempt this segment from death duty (Tallon & al, 1984, p. 11). The Treasury, perturbed by such gratuitous relaxations of the law by the Inland Revenue, put in place a process for overseeing individual and class concessions. Individual concessions above £50 would be furnished yearly to the CAG, together with the reasons for the dispensations (PAC, 1898, p. 148). The CAG would thereafter use his or her ‘discretion with care and tact’ and report to the PAC any particular concession that it was considered ought to be brought to their attention. It was stressed that class concessions, meanwhile, should be put on a statutory footing at the earliest opportunity. Since 1897, the CAG and PAC have concerned themselves with simply questioning why class concessions have not been put on a

statutory footing, rather than analysing whether the concessions were within the discretion of HMRC to grant. They have not, therefore, looked at the consistency of class concessions with the law, whether they are sufficiently clear or whether certain practices should be published. For instance, the CAG in the report for the year ending 31st March 1953 noted the following (CAG, 1953, p. x):

As the remissions still without statutory cover had become rather numerous I asked for information as to the principal concessions which continued in force, and the intentions of the Department with regard to seeking such cover.

In the report for the year ended 31st March 1968, the CAG similarly directed the Revenue towards regularising concessions, rather than analysing the substance (CAG, 1968, p. x):

The Committee of Public Accounts of Session 1966-67 endorsed the view expressed in Treasury Minute of 31 December 1897 that statutory cover should be sought for remissions applicable to classes at the earliest opportunity.

Likewise, in the report for the year ended 31st March 1981, the CAG reiterated the focus of the bodies on placing concessions in legislation, and not on expending time reviewing the interstices of ESCs (CAG, 1981, p. xi):

Over the years successive Committees of Public Accounts have endorsed the view, first expressed by the Treasury in 1897, that wherever possible extra-statutory class concessions should be placed on a statutory footing at the earliest opportunity.

In 1991, the PAC intimated again its unease with published ESCs, but did not apply any scrutiny to the corpus of the existing class concessions (PAC, 1991, p. 71):

We learnt that three concessions which were suitable for legislation were over 50 years old and that one concession which had been classified as temporary was also 50 years old.

What these examples serve to demonstrate is that although the PAC and CAG have been given a specific mandate to scrutinise ESCs, and although the bodies have



nominally noted this in the reports, the bodies have failed to interrogate the relevant ESCs for consistency with the law, clarity or grounds for publication.

### **HMRC soft-law problems manifested in practice**

Given the existence of such a supervisory vacuum, it should be unsurprising that the substance of HMRC soft-law is often riddled with problems. Given that taxpayers turn to soft-law in order to understand their obligations and rights under the law, three problems in particular merit consideration. These are that soft-law in the HMRC is sometimes insufficiently clear, inconsistent with the primary law and lacking in transparency. These will be explored in turn. Of course it should be noted that these problems are not reserved unto tax law, but are intrinsic to the nature of soft-law more broadly.

#### ***Insufficiency of clarity***

As a point of general theory, soft-law ought to supplement the primary law by providing further guidance as to its minutiae, thus rendering the citizen better informed of the legal consequences that will flow from her actions (on which, see: *R. (Purdy) v Director of Public Prosecutions* [2009] UKHL 45, [2010] 1 AC 345 (HL)). That contention is however thwarted where the citizen is denuded of the ability to rely upon the soft-law, for instance, where the soft-law is so vague as to be open to conflicting interpretations. This is precisely what has arisen in the case of HMRC's soft-law publication on the scope of its duty of confidentiality, an example which illustrates the problems which can develop from insufficiently clear soft-law. By way of background, HMRC is bound by a duty of confidentiality enshrined in s. 18 of the Commissioners for Revenue and Customs Act 2005 (CRCA 2005), which provides that 'officials may not disclose

information which is held by the Revenue and Customs in connection with a function of the Revenue and Customs'. The duty is not unrestricted however and exceptions may be made 'for the purposes of a function of the Revenue and Customs' (CRCA 2005, s. 18(2)(a)(i)).

HMRC elaborates on the circumstances in which disclosure of taxpayer information may be made to persons outside HMRC in its Internal Manual 'Information Disclosure Guide'. The guidance states that this information may be disclosed for the purpose of an HMRC function, such as the collection of tax for instance, where the following requirements are satisfied (HMRC, *IDG40415*):

- Failing to do so would result in HMRC being significantly less effective or efficient in carrying out its functions;
- Any detrimental impacts on individuals or legal entities that may result from the disclosure are proportionate to the expected benefits; and
- There are no viable alternatives that could achieve the same outcome without the same (or a similar) level of disclosure.

An example of such a situation, as provided in the Information Disclosure Guide, would be where a tax enquiry could be concluded more quickly by revealing information obtained from a third party. In this instance, it might be judged that disclosure of the information ahead of being required to reveal it by an order in court proceedings would render it likely for the taxpayer to recognise and agree to their true tax liability. This early disclosure would therefore be more resource efficient for both HMRC and the customer.

As may have become apparent, this Manual is quite bare and other than the specific example cited does not make entirely clear under what circumstances HMRC may breach its duty of confidentiality. Whilst it is true that some tolerance in respect of

ambiguous soft-law must be afforded, the ambiguity in relation to this Manual is insufficient for the reason that it gives rise to contradictory positions within HMRC. This state of affairs has become clear in light of the conflicting approaches adopted by HMRC in relation to confidentiality, as revealed by two court cases: *Privacy International v HMRC* [2014] EWHC 1475 and *Ingenious Media v HMRC* [2013] EWHC 3258 (upheld [2015] EWCA Civ 173).

*Privacy International* concerned the power of HMRC to disclose information about its export control functions to an NGO, namely, Privacy International. The NGO alleged that a UK company, Gamma International, had supplied ‘malware’ to repressive regimes in countries such as Bahrain and Ethiopia. It was claimed that Gamma International, in breach of export regulations, supplied the equipment illegally to those states. Accordingly, Privacy International inquired of HMRC, which is obliged to enforce export regulations, whether such equipment had been supplied. HMRC responded that it had no power to provide information about its investigations, by virtue of s. 18 of the CRCA 2005, and that the provision imposed strict controls on the disclosure of information (para 17):

[T]he starting point of this legislation is that without specific legal authority officials of HMRC may not disclose any information held by HMRC in connection with its functions... and it is a criminal offence to reveal any information from which persons... might be identified. Consequently HMRC cannot comment on individual cases, and in particular we will be unable to keep you or other third parties informed of the progress of any investigations.

The tenor of the letter indicated that HMRC’s view was that there were no exceptions that could apply to authorise HMRC to disclose information (para 18). This blanket refusal, the judge pointed out, was misconceived and served as one of the reasons the judge remitted the decision to HMRC to be considered again. Green J cited Sales J’s judgment in *Ingenious Media* from which he extrapolated four separate policy

considerations that HMRC could utilise as justifying its decision to disclose taxpayer information in that case (para 58):

- i. The maintenance of good and cooperative relations with the press;
- ii. Maintaining confidence in the tax system;
- iii. Encouraging the provision of information by taxpayers and the press;
- iv. Deterrence.

*Ingenious Media* concerned an ‘off the record’ disclosure by David Hartnett, then Permanent Secretary of HMRC, to two journalists from *The Times*. The substance of the conversation was of tax avoidance schemes, which were taking advantage of the ‘Film Partnership’ legislative provisions. Over the course of the meeting, Hartnett referred specifically to the appellants, Ingenious Media and Patrick McKenna, as marketers of such avoidance schemes (*Ingenious Media* (CA) para 10); expanded that the appellants had contributed to depriving the public purse of circa £5bn (para 11); that McKenna had personally used such schemes (para 11); and pronounced such schemes as ‘scams for scumbags’ (para 11). Some of these comments were later quoted, albeit with anonymity attached, in an article published by the journalists on the 21st June 2012 (Mostrous, Schlesinger and Watson, 2012). Unsurprisingly, Ingenious Media and McKenna sought judicial review of the decision of Dave Hartnett to disclose such information to *The Times* journalists.

HMRC argued in the case of *Ingenious Media*, with which both the High Court (*Ingenious Media* (HC), paras 38-51) and Court of Appeal (*Ingenious Media* (CA), paras 26-30, and 37-47) agreed, that the disclosure was necessary for the purpose of tax collection. It was accepted that there was a rational connection between the function of HMRC to collect tax in an efficient and cost-effective way and the disclosures made by Mr Hartnett in the course of the briefing (*Ingenious Media* (HC), para [39]; *Ingenious*

*Media* (CA) paras 42-46). It is notable accordingly that in *Ingenious Media*, HMRC contested that it had a relatively wide power to disclose information, whilst in *Privacy International*, the body sought to refuse a request to disclose information on the basis that it had no such power to do so. Such a conflict was not lost on Green J (*Privacy International*, para 60):

The irony of the *Ingenious Holdings* [sic] case as applied in the present case is that in that case the HMRC was arguing for a broad power to disclose information based upon a relatively loose nexus between the information disclosed and the functions of the HMRC and in circumstances where they could be indiscrete and in fact disparaging about both a company (*Ingenious Holdings*) and an individual who promoted tax avoidance schemes. In the present case however HMRC has moved to the absolute other end of the spectrum and in the Decision letter and in subsequent correspondence denied that it has any power at all to disclose information and has adopted a narrow approach towards disclosure which ostensibly contradicts its own arguments in *Ingenious Media*.

Even more disconcerting is the fact that HMRC's standpoint on disclosure in *Ingenious Media* contradicted the previous position advocated by Dave Hartnett before the Public Accounts Committee in 2011. Hartnett's response to questioning around the scope of the duty of confidentiality was that disclosure might in fact *hinder* the efficient collection of tax, thereby somewhat undermining the argument adopted in *Ingenious Media* (PAC, 2011, Ev. 67):

[I]f taxpayers believe that their information may be disclosed, it will make it very much more difficult for us to collect tax.

These apparent conflicting interpretations of the law relating to breaches of confidentiality (Sanitt, 2015, p. 9) appear to be guided by expediency and not principle (*Privacy International*, para 54), as HMRC shifts the goal posts according to the exigencies of the particular predicament. The ambiguity of the internal guidance to an extent allows HMRC to do so. In sum, the problem with this piece of soft-law is that it

can produce conflicting approaches to an area of law which is particularly sensitive for taxpayers, and one which senior members of HMRC have previously acknowledged to be so.

### ***Inconsistency***

As a matter of general constitutional propriety, HMRC is not entitled to usurp the role of Parliament. It must not produce soft-law which is inconsistent with the primary law, although some flexibility must be given in order to allow for administrative discretion. Lord Hoffmann surmised that HMRC's administrative discretion 'enables the commissioners to formulate policy *in the interstices of the tax legislation*' (*R (Wilkinson) v IRC* [2005] UKHL 30; [2006] STC 270 [21] (emphasis added)) but that does not allow the commissioners to concede 'an allowance which Parliament could have granted but did not grant'. To do the latter would be to act *ultra vires*. The rationale behind this constriction is that it prevents HMRC from playing fast and loose with tax legislation and levying persons, parties or goods as the body sees fit. Such a state of affairs would effectively 'reverse the result of the Civil War' (*M v Home Office* [1994] 1 AC 377, 395 (Lord Templeman)). Concessions are an obvious area in which there is potential nevertheless for HMRC to act beyond its powers and overreach the authority of Parliament by issuing soft-law inconsistent with the primary law. The piece of soft-law, ESC 'D33', is a particularly apt example. This is a class concession relating to Capital Gains Tax (CGT).

By way of background, CGT is levied (Taxation of Chargeable Gains Act 1992, s. 1) on any gain (TCGA 1992, s. 15) accruing to a chargeable person (TCGA 1992, s. 2) from the chargeable disposal (TCGA 1992, ss. 21-27) of a chargeable asset (TCGA

1992, s. 21(1)). A chargeable asset in turn is defined in very broad terms as *any form of property*, whether situated in the UK or not, including:

- a) options, debts and incorporeal property generally, and
- b) any currency other than sterling, and
- c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired (TCGA 1992, s. 21(1))

In *O'Brien v Benson's Hosiery (Holdings) Ltd* [1980] AC 562, a director under a seven-year service contract with the taxpayer, Benson's Hosiery, was released from his obligations in return for payment to the taxpayer of £50,000. The House of Lords held that the £50,000 was subject to CGT on the basis that the *contractual right of the taxpayer* to the director's services was an asset which could be and had been turned to account. The case of *Zim Properties v Proctor* [1985] STC 90, which was the catalyst for ESC D33, follows from this case. *Zim Properties* concerned a settlement arrived at between a firm of solicitors and Zim, the taxpayer. Owing to alleged negligence on the part of the solicitors, the sale of three properties fell through. The solicitors settled the matter for £69,000, which the Revenue in turn assessed to tax. In line with *O'Brien*, the court held that a right to bring an action is an 'asset' for the purposes of CGT (TCGA 1992, s. 37(1)), provided such action is not vexatious or frivolous (*Zim Properties*, 106). Further, Warner J held that the capital sum was not derived from any underlying asset, in this case the three properties, but rather from the right of action itself (*Zim Properties*, 108-109).

For taxpayers generally, this case would have a wide-ranging effect. The 'gain' which is subject to CGT is calculated by deducting the acquisition cost (TCGA 1992, s. 38), exemptions (e.g. TCGA 1992, s. 3), reliefs (e.g. TCGA 1992, ss. 222-226) and losses (TCGA 1992, s. 16) from the proceeds of the disposal of the asset. As such, rights

of action would be assessable to tax in their own right and the acquisition cost, statutory reliefs and exemptions relating to a separate, underlying asset would not be deductible. An anomalous position thus arises whereby, taking *Zim Properties* as an example, the £69,000 could not be used for any reliefs or exemptions as it arose from a claim of negligence, but if the firm of solicitors had simply smashed up a property, causing £69,000 in damage, then that sum would be subject to the full range of reliefs and exemptions!

ESC D33 was introduced in 1988 (see: HMRC, 2014, p. 10) to combat this anomaly by extending the range to which an *underlying asset* would be engaged. In other words, despite the strict legal position, the Revenue would treat a cause of action relating to an underlying asset as being derived itself from the underlying asset and thus eligible for statutory reliefs and exemptions in connection with the asset. The chargeable gain would be significantly reduced by virtue of the ability to deduct the acquisition cost and apply lucrative reliefs (HMRC, 2015, paras 8-10). HMRC has claimed that this extension of the range to which what will qualify as an underlying is supported by the case of *Pennine Raceway Ltd v Kirklees Metropolitan Council (No 2)* [1989] STC 122 wherein Pennine Raceway held a licence to conduct drag racing on a disused airfield. When Kirklees Metropolitan Council rejected planning permission, the value of the licence dropped. The Council paid compensation to Pennine and the Court of Appeal held that this compensation reflected the loss in value of the licence. But there is a clear distinction between these two instances. There is no doubt that the licence in *Pennine Raceway* represented an underlying asset and the impact of not obtaining planning permission would have been to reduce the value of the licence. The example accordingly is of false equivalence and cannot serve as the basis for extending the range to what will qualify as an underlying asset.



To reiterate Lord Hoffmann's appraisal, a concession may only be granted within the interstices of legislation, but cannot relieve tax which Parliament has prescribed as due. Could the concession here then be characterised as mere purposive interpretation and as such legitimate? The answer to this question must equally be in the negative, as the success of that argument hinges on some ambiguity in relation to the meaning of the legislative text. But the High Court in *Zim Properties* clearly set out that the capital sum may derive from the right of action itself and so, this argument must make way for the ultimate conclusion that the concession is ultra vires by reason of its ambition to overrule a judicial decision (on which, see also: Southern, 2015, p. 6).

Similarly controversially, where a right of action arises that does not involve an underlying form of property, the ESC holds that any gain accruing on the disposal of the right of action would be exempt from capital gains tax (HMRC, 2015, para 11). The argument for purposive interpretation again is moot given that this paragraph cuts entirely against the decisions in *Zim Properties* and in *O'Brien* that a right of action is an asset for CGT purposes. HMRC has argued however that the concession was justified initially on grounds of administrative convenience (HMRC, 2014, p. 13). That might be persuasive in the case of a negligible amount of compensation. When the concession was introduced in 1988 however, there was no limit to the amount that would be exempt from CGT. In January 2014, HMRC set a limit of £500,000 below which there would be no question of CGT. It is, candidly, impossible to foresee any circumstance in which the administrative cost and inconvenience of collecting gains of up to £500,000 would outweigh the benefit. The ultimate problem for HMRC in relation to ESC D33 is that a right of action is recognised as an asset for the purposes of Capital Gains Tax. To this end, the concession seeks to carve out an exception to the general rule and this might go some way to explaining why HMRC are finding it so difficult to

legislate ESC D33.<sup>1</sup> It is an example of HMRC issuing a concession to provide relief contrary to Parliamentary intent.

### ***Publication***

A strong argument can be made to the effect that all soft-law which affects classes of taxpayers ought to be published. Publication gives general assurance to citizens that there is no discriminatory treatment between those who come within the same rule (KC Davis, 1971, p. 110; *UK Uncut Legal Action v HMRC* [2013] EWHC 1283, para 65), thereby increasing confidence in the system by demonstrating that there are ‘no favourites and no sacrificial victims’ (*IRC v National Federation of Self-Employed and Small Businesses Ltd* [1982] AC 617, p. 651). Publication also ensures greater visibility, thereby supporting the role of oversight bodies, who can analyse the legality of the soft-law and also test administrative action against the published policy, to ensure fairness of application (Craig, 2012, p. 469). Publication provides a safeguard whereby the material is open to examination by interested parties, consultation and critique (Craig, 2012, p. 471). Additionally, where soft-law rules are unpublished, their legal status ‘may be unclear’ (Craig, 2012, p. 469) and the relevant decision-maker will be unsure how much weight to attach to the soft-law at issue. In theory, publication should not be necessary, as HMRC is required to tax a person in accordance with a particular practice even if the taxpayer is unaware of the practice (*J Rothschild Holdings v IRC* [1988] STC 645, p. 665g), provided that the practice is within HMRC’s powers. However, this theoretical basis only holds in reality where a taxpayer approaches HMRC who in turn then applies the treatment. Apart from such an exceptional circumstance, the taxpayer will fail to obtain the relief to which she or he is entitled (Troup, 1992, pp. 134-135).

Nevertheless, as regards publishing soft-law and, particularly concessions, the history of the Inland Revenue merits criticism. Practitioners have written about many instances where HMRC has offered class concessions which are not published (Nolan, 1981; Booth, 1998, p. 180). Additionally a glut of previously unpublished concessions have come to light in the past decade or so (e.g. HMRC, 2009a, p. 13; HMRC, 2008, pp. 5-6). By way of example, an unpublished concessionary practice which operates today relates to pupil barristers. The concession, published *only* in Bar Council guidance and not in an HMRC publication, allows pupils to treat payment for the first six months of pupillage to be treated as tax-free (Bar Council, 2012).

### **Contribution by the Ombudsman to the oversight of HMRC soft-law**

Before proceeding to the discussion of the merits of oversight by the Ombudsman, it is first necessary to provide a general overview of the operation of the Ombudsman by reference to the office's remit, powers and influence. The Ombudsman is an officer of the House of Commons and is appointed by the Crown on the advice of the Prime Minister. In practice, the appointment follows from consultation with the Chair of the Public Administration and Constitutional Affairs Committee (PASC) and approval by the leader of the opposition (Harlow and Rawlings, 2009, p. 530; Wade and Forsyth, 2014, p. 71). The Ombudsman's remit, drafted in very broad terms, is to investigate complaints of 'maladministration' by government departments and some other public bodies (Parliamentary Commissioner Act 1967, s. 5(1)(a)) including HMRC (PCA 1967, s. 4, Sch. 2) causing 'injustice' to a member of the public (PCA 1967, s. 5(1)(a)). Both 'injustice' and 'maladministration' are not defined, although a broad approach is generally taken to the question of what constitutes maladministration causing injustice

(Harlow and Rawlings, 2009, p. 533; Wade and Forsyth, 2014, p. 74; Seneviratne, 2002, pp. 45-46).

The utility of the office is ensured by its wide powers of investigation (Kirkham, 2007, p. 6). The officer has almost unfettered access to papers and persons, a 'striking advantage' of the Ombudsman over MPs' questioning (KC Wheare, 1971, p. 144). The officer may effectively compel any Minister, officer, member, or person related to the purportedly offending department to furnish information or produce documents (PCA 1967, s. 8(1)). As the investigation takes place in private, any secrecy or confidentiality condition of that person's employment is obviated (PCA 1967, s. 8(3)), except in relation to Cabinet proceedings (PCA 1967, s. 8(3)). The Commissioner has the same powers as the Court to summon and examine witnesses (PCA 1967, s. 8(2)). However, the Minister concerned may give written notice to the Ombudsman that disclosure of certain documents or information would be prejudicial to the safety of the State or otherwise contrary to the public interest (PCA 1967, s. 11(3)). This power has rarely been used in practice (Kirkham, 2007, pp. 12 and 24).

Reports on the investigations carried out by the Ombudsman are laid before the PASC (PCA 1967, s. 10(4)), whilst individual findings and recommendations are dispatched to the referring MP (PCA 1967, s. 10(1)). Although the Ombudsman holds no formal powers to compel compliance with any of the office's recommendations, the involvement of the PASC (Harlow and Rawlings, 2009, p. 534) and referring MP (Wade and Forsyth, 2014, p. 69) is generally sufficient to ensure compliance on the part of the offending public body. As Roskill LJ noted in *Congreve v Home Office* [1976] QB 629, 'no criticism of a government department could be more devastating'. In the case of individuals, the recommendations of the Ombudsman, which can range from the issue of an apology (e.g. PCA, 1974b, p. 12) to financial compensation (e.g. PCA,

1974a, p. 106), seek to restore the complainant to the position he or she would have been in had the maladministration not occurred (PHSO, 2008b, p. 377). Recommendations may also be directed towards broader, systemic change (e.g. PCA, 1996, para 54).

The broad jurisdiction of the Ombudsman, the wide-ranging powers and the potency of its investigations combine to render the office well placed to oversee HMRC soft-law. As the supervisory mechanisms which ought to be active as regards HMRC soft-law are almost non-existent and recalling that the catalyst for the Ombudsman's inception was recognition of the inadequacy of the existing apparatus for holding executive action to account, it might come as little surprise that the office has been effective in providing oversight for HMRC's use of soft-law. In particular, empirical evidence demonstrates that the Ombudsman has been efficacious in remedying soft-law failings such as inconsistency with the underlying law, insufficiency of guidance and non-publication.

### ***Inconsistency***

In terms of combatting inconsistency between the law and the soft-law, the Ombudsman has occasionally forced HMRC to change its guidance where it fails to reflect legal advice as to the underlying law. This arose in a case concerning the collection of betting duty from an on-course bookmaker (PCA, 1977, p. 8).

As it stood at the time, possession of a valid betting duty card was necessary before a bookmaker could stand at a race meeting. Before these cards could be issued, the bookmaker had to pay a deposit calculated by reference to estimated duty liability. The complainant in this case, who had held a bookmaker's permit for about fourteen years, received a demand for payment of £35. It was said that he owed betting duty amounting

to over £200 for the previous year and the amount of £35 was required as a deposit if he wished to obtain further betting duty cards while the matter was being investigated. During the course of the investigation, the Ombudsman found that Customs Notice No. 455 (about not issuing cards if all duty due has not been paid) was inconsistent with the Department's legal advice about the circumstances in which they are empowered to refuse to issue a card. Subsequent to this issue being highlighted, the Department corrected Customs Notice No. 455 so as to properly reflect the underlying legal position. This was that Customs officers were not empowered to refuse the issue of a betting duty card to a bookmaker on the ground of being in arrears with duty payment, but merely to require additional security as a condition of the issue of a card (PCA, 1977, p. 812).

At other times, the Ombudsman has caused HMRC to update its guidance so as to reflect the law as it stands at any given time. For instance, the Ombudsman urged the Inland Revenue to abandon the hardship test in the rules governing the application of (now) ESC A19, which allows for the forgiveness of tax where there are delays on the part of the Department in using information (HMRC, 2015, pp. 21-22). Owing to this pressure, the Inland Revenue relinquished the requirement that the delay must additionally have caused the taxpayer hardship (PCA, 1996, para 37). In other cases, it need not be substantive updates which are needed, but merely procedural ones. In the damning *Tax Credits: Getting it wrong?* report (PHSO, 2007), dealing with the systemic problems encountered following the introduction of Tax Credits, the Ombudsman recommended that HMRC develop feedback mechanisms to enable staff to learn from complaints about the unreasonable application of COP 26 (PHSO, 2007, pp. 12 and 28). This is the Code of Practice which sets out the procedure for remedying overpayment of tax credits (HMRC, 2014). The report also recommended that HMRC

should ensure that proper consideration is given to the impact of recovery decisions on the individuals and families concerned. Both recommendations were accepted (PHSO, 2008a, p. 20). In terms of the latter, HMRC responded by ensuring in future that any time a question of 'hardship' were to arise, it would be put to the Debt Management and Banking Unit in HMRC, who are specialists in determining the question of hardship (PHSO, 2007, pp. 13 and 38).

### *Insufficiency of Clarity*

In combatting the insufficiency of some pieces of soft-law in providing guidance to taxpayers as to their treatment by HMRC, the Ombudsman has likewise intervened at times to good effect. In order so that soft-law has its optimum utility, it is essential that HMRC publications to the general public should not be ambiguous. This was unfortunately what arose in relation to ESC A5 (now obsolete) (PCA, 1987, p. 13). This specified that it was Inland Revenue practice not to assess removal expenses borne by the employer where the employee 'has to change her or his residence' as a result of a transfer to another post within an organisation. This was said only to apply if the employee was forced to travel at least 25 miles or over an hour by public transport. In the case itself, the employee's new office was 20 miles from his residence, but his employer, for commercial reasons, thought it essential for him to live within five miles of the new branch. The Ombudsman did not find that there was maladministration in the case in failing to apply the terms of the concession to the employee in question, but did query the wording of the concession as it failed to make clear the degree of necessity required by the phrase 'has to change [her or] his residence'. Accordingly, the Chairman of the Board of Inland Revenue accepted that the concession was seriously ambiguous and that it needed to be reviewed and improved.

Problems of insufficiency need not only abound in relation to soft-law directed to the public, but can also manifest themselves in internal guidance to department officials. In a case concerning a returning holidaymaker, the Ombudsman found that actions of Customs officials had been contrary to legal advice, but also that the advice to the officials in the case had been fragmented and imprecise (PCA 1982, pp. 16-17). The holidaymaker in question was returning to the UK with furniture, but had improperly completed a declaration form. The question for Customs officials was whether this was ‘reckless’ or ‘careless’, but during the interview, the holidaymaker had not been advised that ‘recklessness’ was being considered. The woman had been given a Rule II caution by the Customs officials, but not a Rule III caution (on which, see: Keane and McKeown, 2013, p. 383), before she was offered the option of court proceedings or payment of a sum to compound proceedings. The proper legal course of action in instances where there have been allegations of recklessness was in fact to refer to the Department’s solicitor, but the officials were not made clear of this. The Department accordingly agreed to make administrative changes in the procedures to shore up these inadequacies in the internal guidance. The case also serves to demonstrate the two-way nature of soft-law - even where it is primarily directed at officials, it can nevertheless impact upon taxpayers.

Another piece of soft-law evidencing this is Code of Practice no. 26 (COP 26). In *Tax Credits: Getting it wrong?*, the Ombudsman recommended that the Department produce a set of clear and comprehensive guidelines on the application of the revised COP 26, together with training for staff in its application and the desired outcomes (PHSO, 2007, p. 39). The revised COP 26 replaced the ‘reasonable belief’ test with a much clearer test of whether the tax credit customer has alerted HMRC to an error or change of circumstances. Previously it was a requirement that it must have been



reasonable for the claimant in question to believe that their payments were correct in order to obtain the benefit of the Code of Practice. The following year, the Ombudsman further forced HMRC to clarify whether COP 26 would be applied retrospectively (PHSO, 2008a, p. 18).

Insufficiency of guidance can also relate to more mundane cases, like that of the complaint concerning an Inland Revenue Valuation Office form. The Inland Revenue took on board the criticism of the Ombudsman that there was an inadequacy of information of the form and endeavoured to review the form accordingly to ensure that it was more straightforward to use (PCA, 1970, pp. 166-167).

### ***Publication***

By having such unencumbered access to internal documents and people, the Ombudsman is well placed to understand internal HMRC guidance and to provoke publication where the guidance enshrines policies, procedures or interpretations which impact taxpayers. By way of example, the Ombudsman's investigations for the year 1991 revealed a previously unpublished extra-statutory practice (PCA, 1991, p. 15). The Inland Revenue was allowing repayments of tax to be made outside the statutory six-year time limit laid down by section 43 of the Taxes Management Act 1970 where the claim is delayed by reason of mistakes made by the Inland Revenue or by another government department. Following the Ombudsman's inquiry into a complaint from a taxpayer who belatedly discovered that he had not received the benefit of old age allowance to which he had an entitlement since the mid-1970 (for which the Inland Revenue made an ex gratia payment of £1,930.17), the Inland Revenue agreed to look into the possibility of publishing the existence of the practice and undertook to ensure that it was promulgated in the Revenue's internal instructions to tax offices. The

concession was subsequently published that year as ESC B41. In another case where a traveller accused Customs officials of having damaged his property when his luggage was being searched at a port of entry, the result of the Ombudsman's investigation was the revision of internal guidance and its publication as a Code of Practice (PCA, 1996, para 67). The particular officials were wearing outer coats thereby concealing their name badges, contravening Customs & Excise guidance (Traveller's Charter). Meanwhile, internal guidance on dealing with complaints was also not followed. Subsequent to this investigation, Customs and Excise modified its internal policy and thereafter published it as 'Complaints and putting things right: our code of practice' in January 1996 (see now, HMRC, 2009b).

### **A new robust supervisory mechanism?**

There is an obvious question which follows from a reading of the previous section. Why not simply empower the Ombudsman to further engage in the role of supervision in relation to HMRC soft-law, thereby vitiating the problems identified in the UK in this paper? Here the limitations of the ombudsman solution with regard to the HMRC are noted.

First, there is the issue that the Ombudsman's *focus* is not upon HMRC soft-law. The above handful of case studies cited were the finest examples of Ombudsman interventions in HMRC soft-law which the author could find from a comprehensive study of all the Ombudsman's annual reports since the office's inception. To this end, the examples are not a general reflection of the work undertaken by the office, but rather a collection of individual instances of admirable interposition. Following from this point, is the more important observation that the examples cited arose tangentially out of Ombudsman investigations. The Ombudsman's focus is upon remedying general

administrative deficiencies within public bodies which have caused individuals injustice (Oliver, 1978, p. 452). That the office has at times in its history remedied problems in relation to HMRC soft-law is not deliberate, but serendipitous. It would be misconceived accordingly to believe that simply urging the Ombudsman to take greater control of HMRC soft-law issues would provide the redress that is required. Rather what would be required would be the establishment of a separate department within the Ombudsman's office which solely focused upon matters of HMRC soft-law. This department would in turn have to be endowed with extra resources in terms of staff, expert training and funding. Reforms of this sort to the office seem infeasible, although reform itself is not off the cards as there is ongoing debate more generally as to the desirability of merging several ombudsman schemes with a Bill scheduled for this summer/autumn (Maer and Everett, 2016, p. 3). As it stands, HMRC already accounts for a substantial proportion of the Ombudsman's resources. It is regularly the second most complained of department and ranks consistently in the top 5 for government departments in terms of complaints taken for formal investigation (PHSO, 2012, p. 17; PHSO, 2011, p. 14; PHSO, 2010, p. 22; PHSO, 2009, p. 28; PHSO, 2008a, p. 11; PHSO, 2007, p. 8; PHSO, 2006, p. 9). To expect that HMRC soft-law should be further assigned a disproportionate share of the Ombudsman's resources does not appear to be realistic.

A second significant hurdle is the *remit* of the Ombudsman in its current form. Its jurisdiction would have to be stretched, or would have to be amended, in order to fully take on the supervisory role in respect of HMRC soft-law. Firstly, the Ombudsman is supposedly constrained to the extent that it cannot question the merits of HMRC decisions (PCA 1967, s. 12(3)). However, the case studies demonstrating the effectiveness of the Ombudsman in supervising HMRC soft-law largely involve

questioning the discretionary judgments underlying the interpretations in the relevant soft-law. Thus, the effectiveness of the Ombudsman has been founded upon a blurring of its jurisdictional boundaries. Put another way, soft-law is not an area *per se* that the Ombudsman is entitled to investigate and it would not be sensible accordingly to seek to continue to overstep this boundary by putting greater pressure on the Ombudsman to interrogate soft-law. Moreover, in order to fully function as a supervisory body in respect of HMRC soft-law, it would be necessary to remove the requirement that there is an individual complaint before action can be taken, the merits of which have been subject to debate (Kirkham, 2007, p. 19), with some proposing for the Ombudsman to have its own powers to initiate investigations. This requirement undermines the effectiveness of a supervisory body in ensuring correctness and clarity of soft-law, in addition to ensuring its publication where relevant to taxpayers. Although individual complaints help to focus the attention of the Ombudsman, the requirement severely curtails the Ombudsman's ability to comprehensively scrutinize HMRC soft-law. Simply because an individual complaint has not reached an Ombudsman does not mean that there are no problems. Further, the requirement is particularly unhelpful in directing the Ombudsman towards soft-law which *ought to be* published, given that an individual cannot know about the existence of any internal guidance for which s/he is not receiving the benefit. Combined, these three jurisdictional issues underline the limitations of the Ombudsman's current remit to act as an effective supervisory body for HMRC soft-law.

Taking the two hurdles of *focus* and *remit* together, the problem of empowering the Ombudsman to further engage in the role of supervision is that it would require the establishment of a new department with a new remit. Whilst this would be possible, it should become apparent that this would effectively result in the creation of a new

institution. As the old adage goes, if it looks like a duck and quacks like a duck, then it probably is a duck. It is unrealistic to expect the Ombudsman to comprehensively plug the holes in the existing framework. To this end, it is surely preferable to accept that there is a need for a new institution rather than trying to do so by the backdoor by tinkering to such an extent with the Ombudsman.

Of course, the Adjudicator's Office acts in an Ombudsman type role in relation to HMRC. The Adjudicator is responsible for complaints in relation to HMRC, the Valuation Office and the Insolvency, and is given an almost identical remit to that of the Ombudsman (Adjudicator's Office, 2013, p. 1) but without the MP filter. Complainants should approach first the Adjudicator before approaching, if still dissatisfied, the Ombudsman through their MP. It is a prior step in the complaints machinery (Adjudicator's Office, 2013, p. 1). To this end, there is, in a sense, an HMRC Ombudsman, but the point remains that it would be unrealistic to expect the Adjudicator to dedicate a disproportionate share of its resources towards overseeing a very specific area of HMRC activity, namely soft-law. It would similarly be stretching the remit of the Adjudicator to have the body overseeing soft-law. The reasons given in the paper that the Ombudsman is not the ultimate answer to the issues identified likewise apply to the Adjudicator accordingly.

Finally, relying on the Ombudsman, or to this end, the Adjudicator, alone for the purpose of oversight has a sort of "closing the stable door after the horse has bolted" feel about it. The Ombudsman *operates ex post* when a problem has already been perceived to have arisen, whilst the current article makes the case that there is a need for some concurrent or *ex ante* control to filter issues before they manifest themselves as errors in soft-law affecting the public. But that is precisely the point. The Ombudsman serves an important constitutional role in providing a crucial link between

the individual citizen and the various institutions of the state. It is a salient constitutional principle that those empowered to provide public services should be accountable to the public for the provision of those services (Kirkham, 2006, p. 129). The Ombudsman acts on behalf of the individual to provide redress or to investigate potential impropriety. In the case of soft-law, the Ombudsman is a form of specialized scrutineer of systemic administrative practice for the citizen. The Ombudsman should continue to operate in such a capacity, in tandem with other institutional reforms. Any reforms to the body itself (see O'Brien, 2015), or to the framework within which soft-law is produced should be cognizant of this function and cautious not to dilute it.

## Conclusion

Whilst there might be 'little rhyme or reason in the existing system' (Harlow and Rawlings, 2009, p. 481), there is certainly merit in the suggestion that the Ombudsman is now a 'venerable institution' (Abraham, Preface to Kirkham, 2007, p. 1). Owing to increasing exploration of the 'flexibility' contained within the governing 1967 statute, the Ombudsman has become a 'valuable tool in the ongoing process of calling the government to account' (Kirkham, 2007, p. 20). Within the office's sprawling ambit have inevitably come HMRC's activities in relation to its promulgated publications and soft-law policies. The Ombudsman has demonstrated, at times, a capacity to alleviate failings in the current framework for HMRC soft-law by both exercising oversight. This demonstrates the benefit of having an expert scrutinising HMRC soft-law to ensure that it is consistent with the underlying law which it is purporting to interpret; is sufficiently clear so as to guide taxpayers; and is published where the soft-law in question impacts upon individuals.

All the same, the lessons from the above review of the Ombudsman's functions suggest that its capacity should not be overstated. It is unrealistic, for reasons of institutional setup and remit, to expect the Ombudsman to comprehensively plug the holes in the existing framework. For these reasons, there is a strong argument that the office of the Ombudsman and the Adjudicator should continue to work in their current capacities but also in tandem with any new institution which might be introduced to fix the ailing system. These bodies serve a discreet and valuable constitutional purpose.

As to what new institution might be required, other systems, such as the Australian regime for the promulgation of Public rulings (on which, see: ATO, 2015), offer some interesting potential reforms. Public rulings are pieces of soft-law promulgated by the Australian Tax Office (ATO) that go through a comprehensive development process before being released in final form. This includes significant public consultation, including publication of drafts, and importantly for present purposes consultation with an independent, expert body made up of lawyers, senior ATO officials and academics.

The history of the Ombudsman then provides food for thought in the establishment of a new structure for combating issues of HMRC soft-law, but not a pre-packaged solution.

## Notes

1. HMRC in July 2014 released a consultation paper in which it sought responses on a proposal to legislate ESC D33 (see: HMRC, *Legislating Extra Statutory Concession D33* (n 146)). The closing date for submissions was 15 September 2014. At the time of writing, however, the next steps towards legislating are still being considered. See: <https://www.gov.uk/government/consultations/legislating-extra-statutory-concession-d33>  
[Accessed 8 April]

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